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IN THE

Supreme Court of the United States

October Term, 1944.

No. 418

FRANCICE NETCHER,
Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SEVENTH CIRCUIT AND BRIEF IN SUPPORT THEREOF.

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PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SEVENTH CIRCUIT AND BRIEF IN SUPPORT THEREOF.

To the Honorable the Supreme Court of the United States:

Francice Netcher, an individual, by her attorney, prays that a writ of certiorari issue to review the judgment of the United States Circuit Court of Appeals for the Seventh Circuit entered in the above entitled cause on June 8, 1944, reversing a decision of the Tax Court of the United States.

OPINIONS BELOW.

The memorandum opinion of the Tax Court of the United States is unreported but is contained in the transcript of record, pages 35 to 42, inclusive.

The opinion of the Circuit Court of Appeals (R. 57-65) is unreported but may be found at Par. 62, 594, Vol. 4, 1944 Edition, Prentice-Hall Tax Service.

JURISDICTION.

The judgment of the Circuit Court of Appeals was entered on June 8, 1944. The jurisdiction of this Court is invoked under Section 240(a) of the Judicial Code, as amended by the Act of February 13, 1925 (28 U. S. C. A. § 347).

STATUTES INVOLVED.

The statute and regulations of the Commissioner of Internal Revenue involved are set out in the Appendix, *infra,* (pp. 15-16).

STATEMENT OF FACTS.

The action below was an appeal by the Commissioner of Internal Revenue from the decision of the Tax Court of the United States in which a judgment was rendered in favor of the taxpayer, this petitioner, and a decision of no deficiency in Federal income taxes for the year 1937 was entered on February 12, 1943 (R. 42 and 43).

The petitioner is an individual residing in Chicago, Illinois, and is one of five life beneficiaries of the Trust Estate of Charles Netcher, deceased. The depreciation sustained during the year 1937 by the properties of the trust exceeded the beneficiaries income from the trust with the exception of the beneficiary Townsend Netcher, who had a net income of $200.17 from the trust after his

share of the depreciation on the properties of the estate was subtracted from the amount of income allocable to him under the trust instrument (R. 38).

In computing income tax liability for the year 1937 of the various beneficiaries, the trustee of the trust and the beneficiaries thereof considered that the beneficiaries were entitled under the provisions of Section 23(1) of the Revenue Act of 1936 to deduct or credit against income their proportionate share of the depreciation on the trust assets sustained during the year 1937 (R. 38). The beneficiaries' portion of the depreciation was based on the share of income allocable to each beneficiary under the trust instrument.

The trust instrument involved contained no provision that depreciation should be allowed to the trustee (R. 16-24).

The Commissioner of Internal Revenue determined that the depreciation sustained by the properties of the trust estate during the year 1937 was deductible only by the trustee in computing net income from the estate and refused to allow the beneficiaries to deduct or credit their full proportionate share of the depreciation against income (R. 38).

The Commissioner of Internal Revenue determined deficiencies in Federal income taxes for the calendar year 1937 against this petitioner and the other life beneficiaries (R. 35).

This petitioner and the other beneficiaries appealed to the United States Board of Tax Appeals (now the Tax Court of the United States) from the determination of the Commissioner (R. 35).

The Tax Court filed its memorandum opinion in the case on November 10, 1942 (R. 35-42) and entered a decision

that there was no deficiency in Federal income taxes due from this petitioner for the calendar year 1937 (R. 42).

The Tax Court held that the Commissioner had erred in determining that the trust beneficiaries were not entitled under Section 23(1) of the Revenue Act of 1936 "to credit against their individual income from other sources their proportionate share of depreciation sustained upon the trust assets and in excess of the income from the trust estate" (R. 39).

The Commissioner filed a petition for review by the United States Circuit Court of Appeals for the Seventh Circuit of the decision of the Tax Court of the United States (R. 45-46).

On June 8, 1944, the Circuit Court of Appeals filed its opinion and judgment reversing the decision of the Tax Court of the United States (R. 57).

The Circuit Court of Appeals held that the beneficiaries were not entitled to any deduction for depreciation on the assets of the trust estate and that the deduction for depreciation was allowable only to the trustee (R. 63) even though the trust instrument contained no specific provision for the deduction of depreciation by the trustee and the income from the trust was allocable to the beneficiaries.

QUESTION PRESENTED.

The case presents the question whether under Section 23(1) of the 1936 Act, depreciation deductions are allowable only to the trustee where the trust instrument contains no specific provision granting deductions for depreciation to the trustee and the income from the trust properties is allocated by the instrument to the beneficiaries and not to the trustee.

SPECIFICATION OF ERRORS TO BE URGED.

The Circuit Court of Appeals erred:

1. In deciding that the petitioner and the other life beneficiaries of the trust estate of Charles Netcher, deceased, were not entitled to depreciation deductions for the year 1937, based proportionately on the share of trust income allocated to them by the trust instrument.

2. In deciding that the trustee of the trust estate was entitled to all deductions for depreciation, thus excluding the life beneficiaries of the trust from any depreciation allowances.

3. In failing to hold that the beneficiaries of the trust estate were the owners of an equitable interest in the corpus of the trust property and thus entitled to depreciation allowances.

4. In misinterpreting and misconstruing the provisions of Section 23(l) of the Revenue Act of 1936 and the corresponding sections of all the Revenue Acts beginning with the Act of 1928.

5. In reversing the decision of the Tax Court of the United States.

6. In deciding, contrary to the provisions of Section 23(l) of the 1936 Act and Section 23(k) of the 1928 Act, that relief to the trust beneficiaries must come through Congressional extension of the applicable depreciation provisions even though Section 23(k) of the 1928 Act and the corresponding sections of the subsequent Acts were enacted and reenacted as relief provisions to trust beneficiaries.

REASONS RELIED ON FOR THE ALLOWANCE OF THE WRIT.

1. The decision of the Circuit Court of Appeals herein is in direct confiict with the decision of the Court of Claims of the United States in *Chisholm* v. *United States,* 85 Ct. Cl. 199, 19 Fed. Supp. 274.

2. The decision of the Court below is in direct conflict with the decision of the United States Circuit Court of Appeals for the Second Circuit in *Commissioner of Internal Revenue* v. *Edna C. Gutman,* affirming *Edna C. Gutman* v. *Commissioner,* 1 Tax Court 365, and approving the interpretation of the pertinent section of the statute by the Tax Court. This decision is unreported but may be found at Para. 62, 585, Vol. 4, 1944 Edition, Prentice-Hall Tax Service.

3. The decision of the Circuit Court of Appeals is not in accordance with the decisions of this Court in *Freuler* v. *Helvering,* 291 U. S. 35, 54 S. Ct. 308 and *Helvering* v. *Falk,* 291 U. S. 183, 54 S. Ct. 353.

4. The Circuit Court of Appeals has decided an important question of Federal tax law which has not been but should be settled by this Court.

The Court below has placed an entirely new interpretation upon Section 23(1) of the Revenue Act of 1936 and the corresponding sections of the other Revenue Acts. The construction and interpretation of the pertinent section of the statute by the Circuit Court is in direct conflict with the interpretation thereof by the Tax Court of the United States; the Court of Claims of the United States; and the United States Circuit Court of Appeals for the Second Circuit, approving the interpretation of the section by the Tax Court.

BRIEF IN SUPPORT OF PETITION.

I.

The Circuit Court of Appeals Has Decided an Important Question of Tax Law Which Has Not Been But Should Be Settled By This Court.

Section 23(1) of the Revenue Act of 1936 (Appendix, infra) contains the same provisions as Section 23(k) of the Revenue Act of 1928.

The legislative history of the depreciation provisions of the Revenue Acts as relating to life tenants and life beneficiaries is fully set forth by the United States Board of Tax Appeals in *Sue Carol* v. *Commissioner*, 30 B. T. A. 443 at page 445.

After reviewing the legislative history of the depreciation provisions of the statute and the reasons for the enactment of Section 23(k) of the 1928 Act, the Board of Tax Appeals declared as follows in deciding the case of *Sue Carol* v. *Commissioner, supra* (30 B. T. A. at page 447):

> "From the legislative history above set forth, it is clear that Congress intended to grant to both life tenants and beneficiaries under trust instruments the same privilege of deducting the depreciation allowance as that enjoyed by any other individual. The allowance to the income beneficiary, however, was subject to any *specific provisions relating thereto* which might be contained in the trust instrument, or, lacking any such provision, *to any division of trust income designated therein.* The section has no other limitations whatever to the income beneficiary's right to the depreciation allowance." (Italics ours)

It is the position of the petitioner that the Board of Tax Appeals correctly construed the pertinent section of the statute and that the Court below erred in holding that

trust beneficiaries must seek relief from the hardship imposed upon them under the Court's decision by seeking Congressional extension of the applicable depreciation provisions (Court's opinion, R. 64).

The decision of the Board in *Carol* v. *Commissioner, supra,* was acquiesced in by the Commissioner of Internal Revenue in Cumulative Bulletin XIII-2, p. 4 (1934).

Section 23(k) of the 1928 Act has been reenacted in the subsequent Revenue Acts without any substantial change. The section appears in the 1936 Act as Section 23(1).

The Commissioner did not seek an interpretation of the pertinent section by the Courts following the Carol case and the decision of the Court of Claims in *Chisholm* v. *United States,* 85 Ct. Cl. 199, 19 Fed. Supp. 274, until he appealed from the decisions of the Tax Court in the case at bar (R. 43) and *Edna C. Gutman* v. *Commissioner,* 1 Tax Court 365.

In the instant case the Tax Court of the United States reiterated and approved its previous construction of Section 23(k) of the 1928 Act and relied on its decision in the Carol case as entitling the beneficiaries here involved to the deductions for depreciation (R. 39).

In *Edna C. Gutman* v. *Commissioner, supra,* (1 Tax Court 365) the Tax Court again reiterated and approved its previous construction and interpretation of the section.

Upon appeal by the Commissioner, the United States Circuit Court of Appeals for the Second Circuit affirmed the Tax Court in *Commissioner* v. *Edna C. Gutman,* Para. 62585, Vol. 4, 1944 Edition Prentice-Hall Tax Service.

The Court of Claims of the United States reached the same conclusions as the Board of Tax Appeals in construing Section 23(k) of the Revenue Act of 1928. *Chisholm* v. *United States, supra* (85 Ct. Cl. 199, 19 Fed. Supp. 274).

In the Chisholm case, the Court of Claims relied on the decisions of this Court in *Freuler* v. *Helvering*, 291 U. S. 35, 54 S. Ct. 308, and *Helvering* v. *Falk*, 291 U. S. 183, 54 S. Ct. 353.

In his concurring opinion in *Chisholm* v. *United States*, *supra*, Judge Green said:

> "* * * In the case before us, property was willed to trustees with directions to pay the income over to the plaintiff during his lifetime. This income was to be paid currently and the trustees could make no deductions from it except for administrative expenses and in accordance with the will. The trustees who held the legal title were not taxable upon this income because it was not theirs but that of the plaintiff fiduciary. If he cannot take a deduction for depreciation, no one can. Surely such an inequitable result was not intended by Congress and I find nothing in the statutes which even inferentially indicates such an intention. * * * "

The Court below has placed an entirely new interpretation upon Section 23(1) of the Revenue Act of 1936 and correspondent sections of the other Revenue Acts.

The trust instrument here involved contained no specific provision that the depreciation allowances should be granted to the trustee (R. 16-23). The Court below concluded that there was no specific provision in the will granting all depreciation deductions to the trustee (R. 61 and 64) but the Court held that the will in effect "though not in exact words" provided that the depreciation deduction belonged to the trustee even though the building upon which the depreciation was taken was constructed long after the testator died (R. 58).

The will did contain specific provisions that the income from the trust property should be paid to the beneficiaries; not the trustee (R. 16, 17, 38).

The Court held that the entire deduction for depreciation on the trust property should be granted to the trustee and that the beneficiaries could take nothing by way of depreciation (R. 63).

The decision of the Court below ignores the previous interpretations of the pertinent sections of the statute in the cases named above, viz. that the allowance of depreciation to the beneficiary "is subject to any *specific* provision relating thereto which might be contained in the trust instrument, or, lacking any such provisions, to *any division* of trust income" designated in the trust. (Italics ours.)

The Court's decision overlooks the decisions of the Board of Tax Appeals and the Courts cited hereinabove, that depreciation deductions should follow the allocation of income and that beneficiaries taxable on income should receive the corresponding deduction for depreciation. Under the decision of the Court below, all wills will have to be construed to determine the intention of the testator and the lack of specific provisions and the allocation of income under the trust instrument will have to be ignored.

The decision of the Circuit Court of Appeals returns the situation to its status in 1928 when Section 23(k) was enacted to relieve beneficiaries. (See *Carol* v. *Commissioner*, 30 B. T. A. 443, at pages 446 and 447.). Certainly under the Court's decision life tenants and beneficiaries under trust instruments cannot enjoy the same privilege of deducting depreciation as that enjoyed by any other individual. This is contrary to the intent of Congress in enacting Section 23(k) of the 1928 Act; *Carol* v. *Commissioner, supra* (30 B. T. A. at page 448).

We believe that the Circuit Court of Appeals realized the effect of the decision for the opinion pointed out that the only remedy for beneficiaries would be by Congressional extension of depreciation deductions (R. 64).

The question here involved is of particular importance to all life tenants and life beneficiaries under trusts which own property subject to depreciation allowances. The importance of the issue is illustrated by the fact that the Commissioner appealed from the decision of the Tax Court in Edna C. Gutman, *supra*, although the tax amounted only to $886.01 for the year 1937 and $476.68 for 1938.

The Court below also realized the importance of the question for it said (R. 62):

> "This conclusion, however does not settle the matter. The amendment to the statute and the regulation thereafter promulgated, both quoted above, still leave a *vexatious* question to be determined.
>
> "The Act of Congress here determinative was enacted to permit either a beneficiary of a trust of the trustee of a trust, or both, to use the depreciation deduction, under specified circumstances, to reduce taxable income of said parties.
>
> "The controversy therefore narrows itself down to a construction of the statute, which, in turn, involves the words 'allocable" and 'apportioned' as they appear in the last sentences of the statute as amended. Also debatable, though not controlling, are the words 'in full' as used in the last sentence of Treasury Regulations 94." (Italics ours.)

Accordingly it is respectfully submitted that this case involves an important question of tax law which should be settled by this Court.

II.

The Decision of the Court Below is In Conflict With Decisions of Other Courts.

As pointed out under Point I hereinabove, we believe that the decision of the Circuit Court of Appeals is in direct conflict with the decision of the Court of Claims of the United States in *Chisholm* v. *United States, supra*

(85 Ct. Cl. 199, 19 Fed. Supp. 274) and also in direct conflict with the decision of the Circuit Court of Appeals for the Second Circuit in *Commissioner* v. *Edna C. Gutman, supra* (Para. 62,585, Vol. 4, 1944 Edition, Prentice-Hall Tax Service), affirming *Edna C. Gutman* v. *Commissioner, supra* (1 Tax Court 365).

III.

The Decision of the Circuit Court of Appeals Is Not In Accordance With Decisions of This Court.

The will creating the trust here involved provided that the petitioner and the other beneficiaries of the trust were to receive during their respective lives the net income of the property held in trust (R. 16-17).

Thus the petitioner and the other beneficiaries became the owners of an equitable interest in the corpus of the trust property. *Blair* v. *Commissioner of Internal Revenue,* 57 S. Ct. 330, 300 U. S. 5, and cases cited therein.

Since there was no specific provision in the will providing that the trustee should take all deductions for depreciation or that income should be allocated to the trustee, the beneficiaries as owners of an equitable interest in the corpus of the trust properties were entitled to the deductions for depreciation. *Freuler* v. *Helvering,* 291 U. S. 35, 41, 54 S. Ct. 308; *Helvering* v. *Falk,* 291 U. S. 183, 186, 54 S. Ct. 353.

The decision of the Court below ignores the fact that under the decisions of this Court cited above, the beneficiaries became the owners of an equitable interest in the trust properties; were to receive the income therefrom; and accordingly were entitled to their proportionate share of depreciation deductions.

In *Chisholm* v. *United States, supra,* the Court of Claims relied on the decisions of this Court in *Freuler* v. *Helver-*

ing, supra; Helvering v. *Falk, supra,* and *Blair* v. *Commissioner of Internal Revenue, supra,* in deciding that the beneficiary and not the trustee was entitled to the depreciation deduction.

It is therefore respectfully submitted that the decision of the Court below is not in accordance with the decisions of this Court in *Freuler* v. *Helvering, supra,* and *Helvering* v. *Falk, supra.*

Counsel for petitioner certifies that in his opinion this petition is well founded and is not interposed for delay.

It is respectfully submitted that this petition should be granted.

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APPENDIX.

Revenue Act of 1936, c. 690, 49 Stat. 1648:

Sec. 23. *Deductions from gross income.*

In computing net income there shall be allowed as deductions:

* * *

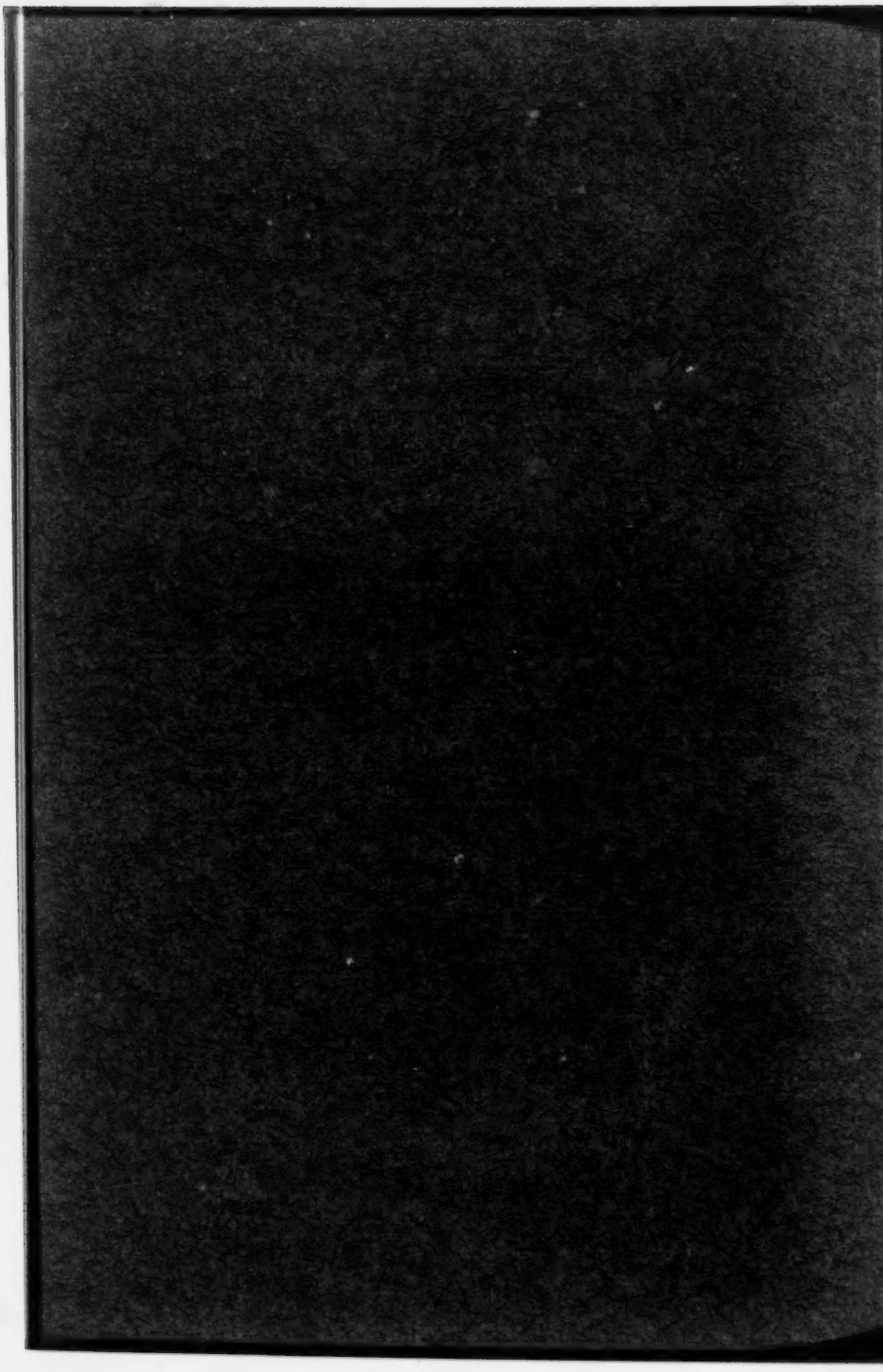
(1) *Depreciation.* — A reasonable allowance for the exhaustion, wear and tear of property used in the trade or business, including a reasonable allowance for obsolescence. In the case of property held by one person for life with remainder to another person, the deduction shall be computed as if the life tenant were the absolute owner of the property and shall be allowed to the life tenant. In the case of property held in trust the allowable deduction shall be apportioned between the income beneficiaries and the trustee in accordance with the pertinent provisions of the instrument creating the trust, or, in the absence of such provisions, on the basis of the trust income allocable to each.

* * *

Treasury Regulations 94, promulgated under the Revenue Act of 1936:

Art. 23 (1)-1. *Depreciation.*— . . . In the case of property held by one person for life with remainder to another person, the deduction for depreciation shall be computed as if the life tenant were the absolute owner of the property so that he will be entitled to the deduction during his life, and thereafter the deduction, if any, will be allowed to the remainderman. In the case of property held in

trust, the allowable deduction is to be apportioned between the income beneficiaries and the trustee in accordance with the pertinent provisions of the will, deed, or other instrument creating the trust, or, in the absence of such provisions, on the basis of the trust income which is allocable to the trustees and the beneficiaries, respectively. For example, if the trust instrument provides that the income of the trust computed without regard to depreciation shall be distributed to a named beneficiary, such beneficiary will be entitled to the depreciation allowance to the exclusion of the trustee, while if the instrument provides that the trustee in determining the distributable income shall first make due allowance for keeping the trust corpus intact by retaining a reasonable amount of the current income for that purpose, the allowable deduction will be granted in full to the trustee.



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In the Supreme Court of the United States

OCTOBER TERM, 1944

No. 418

FRANCICE NETCHER, PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SEVENTH CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

OPINIONS BELOW

The memorandum opinion of the Tax Court (R. 35–42) is unreported.[1] The opinion of the Circuit Court of Appeals (R. 57–64) is reported in 143 F. 2d 484.

[1] In the Tax Court, this case was consolidated (R. 2, 35) with *Ethel Netcher Chagnon* v. *Commissioner* (T. C. No. 107723); *Mollie Netcher* v. *Commissioner* (T. C. No. 107724); *Townsend Netcher* v. *Commissioner* (T. C. No. 107725); and *Irving Netcher* v. *Commissioner* (T. C. No. 107726). Appeals to the Circuit Court of Appeals for the Seventh Circuit have been taken in all of these cases except *Ethel Netcher Chagnon* v. *Commissioner;* but, by order of that court, filed June 23, 1943 (R. 47–48), only the record in the present case was printed; further proceedings in the other cases are to await the final outcome of the instant litigation.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered June 8, 1944 (R. 65). The petition for a writ of certiorari was filed September 1, 1944. The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED

Whether the income beneficiaries of a certain trust are entitled under Section 23 (l) of the Revenue Act of 1936 to an allowance for depreciation on trust assets not absorbed by the trust income, where the trust instrument, as construed by the Tax Court and the court below, required that the trustee, in determining the distributable income, should withhold an amount sufficient to offset depreciation.

STATUTE AND REGULATIONS INVOLVED

Revenue Act of 1936, c. 690, 49 Stat. 1648:

> SEC. 23. DEDUCTIONS FROM GROSS INCOME.
>
> In computing net income there shall be allowed as deductions:
>
> * * * * *
>
> (l) *Depreciation.*—A reasonable allowance for the exhaustion, wear and tear of property used in the trade or business, including a reasonable allowance for obsolescence. In the case of property held by one person for life with remainder to another person, the deduction shall be com-

puted as if the life tenant were the absolute owner of the property and shall be allowed to the life tenant. In the case of property held in trust the allowable deduction shall be apportioned between the income beneficiaries and the trustee in accordance with the pertinent provisions of the instrument creating the trust, or, in the absence of such provisions, on the basis of the trust income allocable to each.

* * * * *

Treasury Regulations 94, promulgated under the Revenue Act of 1936:

ART. 23 (l)–1. *Depreciation.*— * * * In the case of property held by one person for life with remainder to another person, the deduction for depreciation shall be computed as if the life tenant were the absolute owner of the property so that he will be entitled to the deduction during his life, and thereafter the deduction, if any, will be allowed to the remainderman. In the case of property held in trust, the allowable deduction is to be apportioned between the income beneficiaries and the trustee in accordance with the pertinent provisions of the will, deed, or other instrument creating the trust, or, in the absence of such provisions, on the basis of the trust income which is allocable to the trustee and the beneficiaries, respectively. For example, if the trust instrument provides that the income of the trust com-

puted without regard to depreciation shall be distributed to a named beneficiary, such beneficiary will be entitled to the depreciation allowance to the exclusion of the trustee, while if the instrument provides that the trustee in determining the distributable income shall first make due allowance for keeping the trust corpus intact by retaining a reasonable amount of the current income for that purpose, the allowable deduction will be granted in full to the trustee.

STATEMENT

The Tax Court found the following facts (R. 35–38):

The taxpayers, Ethel Netcher Chagnon,[2] Townsend Netcher and Irving Netcher, are children of Charles Netcher, who died on June 19, 1904, a resident of Cook County, Illinois. The taxpayers, Francice Netcher and Mollie Netcher, are children of Charles Netcher, Jr., who died on November 4, 1931, and who was also a child of the above-mentioned Charles Netcher. (R. 35.)

By the will of Charles Netcher, the bulk of his entire estate was left in trust to his widow, Mollie Netcher, now Mrs. Mollie Netcher Newbury. One-third of the net income from the trust estate was to be paid to her for life, with the power by her will or deed to dispose of the right to such

[2] As indicated in the previous note, no appeal has been taken in the case of Ethel Netcher Chagnon.

income from the date of her death to the termination of the trust. The income from the remaining two-thirds of the estate was to be divided by the widow, as trustee, into four equal portions, each of such portions to be thereafter held in trust by the trustee as a separate trust fund for each of the testator's children. (R. 36.)

The will further provided that until each of such children attained the age of 25 years, the trustee should use and expend so much of each separate trust fund held for each child as in her opinion was necessary for the education and support of such child. On attaining his twenty-fifth year, each child was to become entitled to receive the entire income from the separate trust and also to become entitled thereafter to one-fourth of the net income of the above-mentioned two-thirds of the principal trust estate. The trust was not to terminate until the death of the last survivor of the decedent's widow and his four children.[3] In case of the death of one of the decedent's children leaving issue, the latter were to take the interest of the parent subject to an annuity payable to the widow of the deceased child. (R. 36.)

One of the assets included in the trust *res* was certain real property in Chicago, Illinois. Following the testator's death, the widow, acting as

[3] This finding seems incorrect, since the will expressly provides (R. 20) for termination when all the children have died and the youngest living grandchild has reached the age of 21.

trustee under the will, borrowed the necessary funds and erected on this property a seventeen-story fireproof store and office building at a cost of $5,714,759.52, which was thereupon leased to the Boston Store. (R. 36.)

For the calendar year 1937, the sum of the charges for ground rent, interest on mortgage, taxes, and depreciation on the building exceeded the rents by the sum of $102,843.50. This deficit was treated as part of the expenses of the so-called principal trust. The charge for depreciation was an allowance for the loss sustained through exhaustion, wear, and tear of the building and in computing the distributed income of the trust the trustee has continuously deducted from the gross income of the principal trust estate an allowance for depreciation of this asset and has set up a reserve to cover the loss so sustained. The balance in the reserve account on December 31, 1936, was $1,969,676.66, and on December 31, 1937, was $2,112,545.64. (R. 36–37.)

For the year 1937, depreciation sustained on all the properties of the trust estate amounted to $142,868.98, and after the deduction of this amount the principal trust sustained a net loss of $133,993.24 (R. 37).

The Commissioner determined that the depreciation sustained on properties of the principal trust estate in the tax year was deductible only by the trustee in computing net income of the estate, and that any depreciation not thus set off

and consequently reported in the net loss of the estate was not subject to deduction by the individual beneficiaries from income received by them from other sources (R. 13, 38). The Tax Court reversed the Commissioner (R. 39), but the court below set aside the decision of the Tax Court and upheld the Commissioner (R. 64).

ARGUMENT

Section 23 (l) of the Revenue Act of 1936, *supra*,[4] provides that in the case of property held in trust the allowable deduction shall be apportioned between the income beneficiaries and the trustee in accordance with the pertinent provisions of the instrument creating the trust, or, in the absence of such provisions, on the basis of the trust income allocable to each. This provision came into the law in Section 23 (k) of the Revenue Act of 1928, and it has been continued in subsequent acts. Section 23 (k), 1932 Act; Section 23 (1), 1934, 1936, and 1938 Acts and the Internal Revenue Code. The committee reports relating to the 1928 Act (S. Rep. No. 960, 70th Cong., 1st Sess., p. 20 (1939–1 Cum. Bull. (Part 2) 409, 423); H. Rep. No. 1882, 70th Cong., 1st Sess., pp. 11–12 (1939–1 Cum. Bull. (Part 2) 444, 445), contain the following example:

[4] The law was amended in certain respects by Section 121 (c) of the Revenue Act of 1942, but these amendments, although retroactive, are not relevant to the present controversy.

> if the trust instrument provides that the income of the trust computed without regard to depreciation shall be distributed to a named beneficiary, such beneficiary will be entitled to the depreciation allowance to the exclusion of the trustee, while if the instrument provides that the trustee in determining the distributable income shall first make due allowance for keeping the trust corpus intact by retaining a reasonable amount of the current income for that purpose, the allowable deduction will be granted in full to the trustee.

This example was incorporated in the regulations, and it has remained unaltered therein for many years. Article 201, Treasury Regulations 74 and 77; Article 23 (l)–1, Treasury Regulations 86, 94 and 101; Section 19.23 (l)–1, Treasury Regulations 103; Section 29.23 (l)–1, Treasury Regulations 111. It is entitled, therefore, to substantial weight in construing the statute. *Taft* v. *Commissioner,* 304 U. S. 351; *United States* v. *Dakota-Montana Oil Co.,* 288 U. S. 459; *Magruder* v. *Washington, B. & A. Realty Corp.,* 316 U. S. 69.

The court below properly relied upon the example (R. 63) in holding that the deduction is allowable in full to the trustee and not to the beneficiaries. The will, although containing no specific provision as to depreciation, provides that the real estate should be held together for the benefit of the entire estate and the benefici-

aries thereunder. The beneficiaries for many years took the view that their distributive shares should be reduced by depreciation, and in an earlier case relating to their income taxes for the years 1923 to 1925 (*Newbury* v. *Commissioner,* 26 B. T. A. 101), the Board of Tax Appeals so held, and the Commissioner acquiesced (XI–2 Cum. Bull. 7 (1932)). Indeed, such decision might well be considered determinative of the present controversy under the doctrine of *res judicata* (*Tait* v. *Western Md. Ry. Co.,* 289 U. S. 620; *United Shoe Mach. Co.* v. *United States,* 258 U. S. 451, 459) because the question of construction there decided is also determinative of the issue here presented, even though the tax years and statutory provisions are different.

Under these circumstances there is little merit in the taxpayer's contention that the deduction should be split between the trustee and beneficiaries so as to give to the beneficiaries the right to deduct from their income derived from other sources such part of the depreciation as is not needed by the trustee as an offset to trust income. The cases relied upon in the petition are distinguishable on their facts, and there is no conflict. In *Chisolm* v. *United States,* 19 F. Supp. 274 (C. Cls.), the beneficiary was held entitled to the entire deduction. There, however, the trust instrument as construed by the court provided for distribution of the trust income to the beneficiaries

without a deduction for depreciation. Here the trust instrument provides in effect that the trustee in determining distributable income should withhold an amount sufficient to offset depreciation. In *Commissioner* v. *Gutman,* 143 F. 2d 201 (C. C. A. 2d), the court held that the income in question could never become part of the corpus, or be allocable to anyone other than the beneficiary; the beneficiary was held to be entitled, therefore, to the depreciation deduction. In *Carol* v. *Commissioner,* 30 B. T. A. 443 (Acq., XIII–2 Cum. Bull. 4 (1934)), the beneficiary was entitled to the entire income without deduction for depreciation, and hence was entitled to take deduction of the depreciation in the trust property, regardless of the fact that in the particular tax year there was no income therefrom. *Helvering* v. *Falk,* 291 U. S. 183, held only that the beneficiaries receiving royalties from mineral property could deduct under earlier statutes an allowance for depletion representing the return of capital assets.

It is submitted, therefore, that the court below correctly applied the law to the facts here presented, and there is no occasion for further review by this Court. The basic inquiry in this case—whether, under the trust instrument, the trustee had a right and a duty to retain enough from trust income to offset depreciation—turns on the particular facts presented, and is not of general importance. No conflict of decisions is shown.

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted.

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